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No. 151

In the Supreme Court of the United States

OCTOBER TERM, 1939

PEARL E. DEPUTY AND THE SUSSEX TRUST CO., A CORPORATION OF THE STATE OF DELAWARE, AS ADMINISTRATRIX AND ADMINISTRATOR OF THE ESTATE OF WILLARD F. DEPUTY, DECEASED, LATE COLLECTOR OF INTERNAL REVENUE, PETITIONERS

v.

PIERRE S. DU PONT

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE PETITIONERS

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BRIEF FOR THE PETITIONERS

OPINIONS BELOW

The opinion of the District Court (R. 208) is reported in 22 F. Supp. 589. The opinion of the Circuit Court of Appeals (R. 264) is reported in 103 F. (2d) 257.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on March 28, 1939 (R. 268). The peti-

tion for a writ of certiorari was filed on June 28, 1939 and was granted on October 9, 1939 (R. 270). The jurisdiction of this Court is conferred by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether respondent, in computing his net taxable income for the year 1931, was entitled to deduct certain payments made by him in that year to the Delaware Realty and Investment Company either (1) as ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, or (2) as interest paid or accrued within the taxable year on indebtedness.

STATUTE INVOLVED

Revenue Act of 1928, c. 852, 45 Stat. 791:

> SEC. 23. DEDUCTIONS FROM GROSS INCOME. In computing net income there shall be allowed as deductions:
>
> (a) *Expenses.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the

trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

(b) *Interest.*—All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued to purchase or carry obligations or securities (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from taxation under this title.

* * * * *

SEC. 24. ITEMS NOT DEDUCTIBLE.

(a) *General rule.*—In computing net income no deduction shall in any case be allowed in respect of—

(1) Personal, living, or family expenses; * * *.

STATEMENT

This case involves the deductibility, as an ordinary and necessary business expense or as interest paid on indebtedness, of payments made by respondent in 1931 to the Delaware Realty and Investment Company (hereinafter called "Delaware Company"), pursuant to a contract between them, dated October 25, 1929. The nature of this contract and of the payments made thereunder can be understood only by reference to the extended and somewhat complicated history of their origin.

1. *The nature of the payments made.*—The facts are not in dispute, and may be summarized as follows:

The taxpayer became connected with E. I. du Pont de Nemours and Company (hereinafter called "du Pont Company") in 1890. He was treasurer of the company from 1902 until 1915. In 1915 he was elected president and held that position until 1919. In the latter year he retired as president and was elected Chairman of the Board of Directors, which office he has since continued to hold (R. 157, 209).

At the close of the World War, the executives of the du Pont Company realized that there would have to be a substantial change in its business, which up to that time had been chiefly the manufacture of munitions and war supplies. For this purpose it was decided that a new executive committee composed of nine key men in the company, should be formed to function as the general manager of the company. The members of this new executive committee were appointed in the spring of 1919 (R. 209–210). Shortly thereafter respondent, as Chairman of the Board, recommended to the finance committee of the company that a special committee be appointed to take up the question of proper compensation for the members of this new executive committee (R. 210). The recommendation was adopted and a special committee was appointed which considered a number of plans by which the company might properly compensate the members of the executive committee and at the same time give them such a financial interest in

the business as would bind them to the company (R. 210–211). The plan thought most feasible involved, among other things, the transfer to the committeemen of certain shares of stock in the company at a price agreeable to the committeemen and a loan to them by the company of the money with which to pay for these shares. The plan also contemplated the payment by the company of a bonus to the committeemen at the end of a five-year term of service (R. 211). The company's counsel, however, advised that the company had no power to carry out this arrangement because, under Delaware law, stock could not be issued for future services and stock issued for cash had first to be offered for subscription *pro rata* to existing stockholders (R. 211).[1]

In order that the plan would not have to be abandoned because of this difficulty, respondent, at the instance of the du Pont Company, agreed in December 1919 to sell to each member of the executive committee 1,000 shares of common stock at $320 per share, which was approximately the asset value (R. 17, 213, 215).[2] Respondent's purpose in enter-

[1] The du Pont Company did not have the requisite number of shares of treasury stock available for sale to the members of the executive committee (R. 211).

[2] The asset value was below the price at which the stock was then selling on the market, although the market sales were in very small lots (R. 191, 212).

ing into this agreement was not to make a profit out of the specific transactions of sale but rather to conserve and enhance the value of his substantial beneficial stock holdings in the du Pont Company by assuring for the company a stable and efficient management (R. 212–213).

Respondent did not have 9,000 shares of du Pont stock available for delivery to the members of the committee. As a matter of fact, he owned at that time only 74 shares, although he had a reversionary interest in two trusts which he had created and from which he expected to receive back some 24,000 shares of the stock within the next few years. He was also a substantial stockholder in the Christiana Securities Company (hereinafter referred to as "Christiana"), which was the largest single owner of du Pont stock, owning 183,000 shares of a total of 588,542 issued and outstanding (R. 213).

In order to carry out his agreement with the members of the executive committee, respondent arranged with Christiana to lend him 9,000 shares of du Pont stock, the loan to be secured by collateral consisting of 3,800 shares of Christiana stock (R. 47–49, 213–214).[3] In agreeing to this loan, the directors of Christiana recorded the fact

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[3] Respondent could not have bought 9,000 shares of du Pont stock on the market without greatly increasing the market price. The stock was not then listed on the New York Stock Exchange and the over-the-counter market was very thin (R. 211-212, 214).

[redacted]).

that the loan was made, among other reasons, because it was to the benefit of Christiana as the largest stockholder of the du Pont Company to secure the most efficient managerial service for the du Pont Company (R. 47).

The terms of the loan were in substance that respondent would return an equivalent number of shares to Christiana within a ten-year period and in the meantime would pay to Christiana amounts equal to all dividends declared and paid on the shares borrowed (R. 48–49). Respondent did not enter into this agreement for the purpose of making a profit from the loan (R. 214).

The day after respondent made this contract with Christiana, the finance committee of the du Pont Company held a special meeting and authorized the execution by the company of two contracts with each member of the executive committee. One contract provided for the payment to each committeeman of an annual salary of $30,000, additional compensation based upon a percentage of annual net earnings, a bonus of $150,000 if the committeeman was still in the company's employ as a member of the executive committee at the end of five years, and the payment by the company for a period of five years of premiums on a $150,000 life insurance policy. The second contract provided for a five-year loan of $320,000, bearing interest at the rate of 5 per cent per annum, to be made by the company to each member of the execu-

tive committee for the purpose of enabling him to carry out his agreement to purchase 1,000 shares of du Pont stock from the respondent at $320 per share (R. 69–73, 214–215). The loan was to be secured by a pledge of the stock to be purchased and by an assignment of the $150,000 life insurance policy (R. 71–72).

At the end of December 1919 the whole plan was consummated by the execution of the agreements authorized by the finance committee and by the sale and delivery by the respondent to the committeemen of the 9,000 shares of du Pont stock which he had borrowed from Christiana. At the time of the sale, respondent received $320,000 in cash from each member of the committee, or a total of $2,880,000 (R. 215).

By the early part of 1921, the value of du Pont stock had materially decreased so that it seemed possible that the committeemen, instead of receiving a benefit from the transaction, would sustain a serious loss (R. 91). When this condition appeared, respondent wrote a letter to each of the committeemen in which he set forth the motives which had prompted him to enter into the transaction in the first instance and disavowed any intention to make a profit for himself. He expressed the view that it was important that the members of the committee should be free of worry over the unexpected outcome of their stock purchase and consequently offered to give to each of them 400 shares

of Christiana stock, having a value of $400 per share. This stock was to be deposited as additional collateral for the loan from the du Pont Company to the committeemen, subject, however, to the right of respondent to repurchase the stock at $400 per share at the maturity of the loan. The offer was accepted by each of the committeemen (R. 216–217).

In 1929, at the maturity of the loan from Christiana to respondent, due to stock dividends declared by the du Pont Company during the intervening period and to a split-up of the stock by reduction of its par value, respondent was obligated to return to Christiana 142,212 shares to replace the 9,000 shares which he had borrowed (R. 62–65, 218–219). He did not have this number of shares available for the purpose and therefore arranged for a loan of 142,212 shares from the Delaware Company to discharge his obligation to Christiana.[4] The contract

[4] We take issue with the recitation by the court below of the facts with respect to this transaction. The court intimated that respondent had to make the loan from the Delaware Company because, at the time of the maturity of his loan from Christiana in 1929, the market for du Pont stock was thin and panicky financial conditions prevailed, preventing respondent from purchasing in the market the requisite number of shares to discharge his obligation (R. 266). The statement that the market for du Pont shares was thin was based on a finding of the District Court relating to conditions *in 1919*, not to conditions *in 1929* (R. 214). And the statement that there was a financial panic is true only of the time at which the loan from Christiana matured, i. e., December 23, 1929. As a matter of fact, respondent made the

which he made with the Delaware Company, dated October 25, 1929, stated that the respondent, "while not at this time contemplating the closing of the short sale transaction of December, 1919," desired to terminate his indebtedness to Christiana (R. 99). Respondent agreed to return the shares borrowed from the Delaware Company within ten years after October 25, 1929, and in the meantime to pay to that company amounts equivalent to all dividends declared by the du Pont Company upon the borrowed shares, together with amounts equal to any tax liability imposed upon the Delaware Company because of the receipt of these sums from the taxpayer which would not have been imposed but for the execution of the agreement (R. 98–103). Respondent did not enter into this agreement with the Delaware Company with the intention or purpose of making a profit thereby (R. 219).

In 1931 respondent paid to the Delaware Company $567,648, being an amount equal to the dividends paid during 1931 on the shares which he still owed the Delaware Company,[8] and an additional

loan from the Delaware Company on October 25, 1929—two months before the maturity of the Christiana loan and a few days before the stock market crash of October 29, 1929.

We further take issue with the statement of the court below that the Delaware Company was a "wholly alien" company (R. 267). Although respondent was not a stockholder of the company, it was a corporation owned by members of the du Pont family, and its vice president was Irénée du Pont, respondent's brother (R. 103).

[8] During 1929 the taxpayer returned 300 shares to the Delaware Company, thus reducing his obligation to 141,912 shares (R. 219).

sum of $80,063.56, which was the amount of the federal income tax imposed upon the Delaware Company by reason of the payments which it had received from respondent (R. 219). These are the expenditures claimed as a deduction in the present case.

2. *The nature of respondent's activities during the years in question.*—During the entire period in question, respondent was Chairman of the Board of Directors of the du Pont Company (R. 209). In 1919 he was also a stockholder and director of General Motors Corporation, Chatham and Phoenix Bank, Philadelphia National Bank, Bankers Trust Company and other corporations (R. 220). He was president of General Motors from 1920 to 1924 and was paid a salary of $100,000 a year for his services in that capacity (R. 166–168).[a]

During the years in question respondent maintained offices both in Wilmington, Delaware, and in New York, N. Y., for the conduct of his affairs (R. 221). In 1919 he devoted approximately 50% of his time to his investments, which consisted in large part of du Pont stock. He changed his investments from time to time, but he was not a speculator and had practically no investments in

[a] Respondent's connection with General Motors was largely for the purpose of promoting the interests of the du Pont Company which was a large stockholder in General Motors (R. 221).

brokerage accounts (R. 220–221). During the year 1931, for example, he made only 11 sales of securities, although these were of substantial amounts (R. 26). According to the findings of the District Court, his "business was primarily that of conserving and enhancing his estate" (R. 221).

3. *Proceedings below.*—In his income tax return for the year 1931 respondent deducted as "Interest Paid" the sum of $567,648—the amount of the dividends on the borrowed du Pont stock which he paid to the Delaware Company. He did not, in his return, deduct the $80,063.56 which he paid to the Delaware Company to reimburse it for the federal income tax on the payments received from him, but a deduction for this amount was subsequently claimed (R. 219–220). On audit the Commissioner disallowed both of these deductions and determined a deficiency in tax of $142,466.79 (R. 220). Respondent paid the tax, duly filed a claim for refund, and, after the lapse of six months, instituted the present suit (R. 208–209).[7]

In the District Court respondent urged that the payments to the Delaware Company were deductible on five separate and distinct grounds (R. 226).

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[7] The declaration sets forth another issue in addition to the issue of the deductibility of the payments to the Delaware Company. The disposition of this other issue was agreed upon by stipulation between the parties which provides that the taxpayer is entitled to a judgment of $54,439.52 upon the issue settled by the stipulation and will be entitled to judgment in the sum of $172,351.64 if successful upon the question now before the Court (R. 12–13, 222).

The case was tried by the court without a jury. On February 21, 1938, the District Court filed its findings of fact, conclusions of law and opinion, holding that the payments in question were not deductible (R. 208–243).

Respondent thereupon appealed to the Circuit Court of Appeals for the Third Circuit but confined his appeal to the contention that the payments to the Delaware Company were deductible either (1) as ordinary and necessary expenses paid or incurred in carrying on a trade or business, or (2) as interest paid on indebtedness (R. 253). The court below filed its opinion on March 28, 1939, reversing the judgment of the District Court on the ground that the payments were an ordinary and necessary business expense (R. 264). Having so decided the court below was not called upon, and did not, decide whether respondent was also entitled to deduct the payments as interest paid on indebtedness. However, in his brief in opposition to the granting of a writ of certiorari, the taxpayer stated that, should the writ be granted, both grounds would be urged in this Court in support of the decision of the court below (p. 3). Both contentions will, therefore, be considered in this brief.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred—

1. In holding that the expenditures were proximately or directly connected with taxpayer's as-

sumed business of conserving and enhancing his estate.

2. In holding that the expenditures were "ordinary" expenses in such business..

3. In refusing to consider the transaction as a whole and take into account the history and purpose of the borrowing of the shares.

4. In holding that the conservation of a taxpayer's estate constitutes a business.

5. In holding that Section 23 (a) of the Revenue Act of 1928 permits the deduction of amounts expended for the purpose of conserving and enhancing the taxpayer's estate.

6. In failing to hold that the sums of $567,648 and $80,063.56 were in the nature of capital expenditures which are not deductible from gross income.

7. In reversing the decision of the District Court.

SUMMARY OF ARGUMENT

I

For any one of three reasons respondent is not entitled to a deduction under Section 23 (a) for the payments made to the Delaware company: (A) because respondent's activities in connection with "conserving and enhancing his estate" did not constitute a "business" as that term is used in the statute; (B) because, even if these activities did constitute a business, the payments were not proximately connected with the conduct of that business;

and (C) because, in any event, the payments were not "ordinary and necessary" in character.

A. It is true that the District Court stated in its findings of fact that "The plaintiff's business was primarily that of conserving and enhancing his estate." This statement, however, was not properly a finding of fact but a conclusion of law, since the question of whether there is such a business as "conserving and enhancing" one's own capital is not a question of fact but a matter of statutory construction.

We believe that activities in connection with the prudent investment and reinvestment of one's own capital, as distinguished from the activities of a dealer or trader in securities, can never constitute a "business" within the meaning of Section 23 (a). Practically everyone who has any capital devotes some time and energy to the conservation and enhancement of that capital and to the consideration of the prudence of his investments. In the case of the average investor of moderate means, such investment activity clearly does not constitute a business and its personal character is not changed in the case of a wealthy investor simply because his investments require more time and attention and generate more activity.

The rule established by the court below serves to obliterate the distinction between personal and business expenses. It permits respondents to convert purely personal and capital expenses into ordi-

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nary and necessary business expenses by the simple expedient of treating the conservation of his estate as a business and the cost of deferring liquidation of a personal indebtedness as an expense of that business.

B. Even if the conservation and enhancement of respondent's estate were a business, respondent would be entitled to no deduction because the payments in question were not proximately connected with that business. *Kornhauser* v. *United States*, 276 U. S. 145, 153. It is clear that not every payment which conserves one's estate by deferring liquidation of a personal obligation can be considered as a business expense; the deduction may be had only if the obligation itself was incurred in connection with the conduct of the business.

The obligation pursuant to which the payments here involved were made was incurred in connection with the business of the du Pont Company, not in connection with the business of respondent. This Court has several times pointed out that a stockholder's business must be sharply distinguished from the business of the corporation in which he holds stock. *Dalton* v. *Bowers*, 287 U. S. 404; *Burnet* v. *Clark*, 287 U. S. 410. Respondent participated in the transaction at the instance of the du Pont Company and only after the initial proposal that the company itself carry out the plan was found legally objectionable. Although any benefit to the du Pont Company would also result in enhancing the value of respondent's stock in-

terest in the company, this was obviously a secondary consideration. Respondent was the beneficial owner of but 16% of the stock of the company and, had his primary purpose been to enhance his own capital, he would not have entered into a transaction from which 84% of the benefit went to others. Moreover, when, in 1921, he had the opportunity of closing the transaction at a tremendous profit, he did not avail himself of the opportunity but instead made a substantial gift to the members of the executive committee in order to benefit them, and, through them, the business of the company itself.

C. In any event, the expenses were not "ordinary and necessary" in character. It was neither ordinary nor necessary for the conduct of respondent's "business" of conserving and enhancing his estate for him to have incurred a large liability in order to compensate employees of a company in which he held stock. The burden of providing adequate compensation for the members of the executive committee rested upon the company and respondent does not suggest that the company was financially unable to discharge that obligation. The fact that respondent undertook to assume the burden himself cannot change what would have been an ordinary and necessary business expense of the corporation into an ordinary and necessary business expense of one of its stockholders.

Moreover, the liability with respect to which the payments were made had its origin in a short

sale of securities. Respondent was not in the business of making short sales and knew little about them. And, even as a short sale the transaction was out of the ordinary. The usual short sale is a short-term proposition entered into by a trader or speculator in securities in order to derive a profit out of the specific transaction. Here, respondent borrowed the stock for a period of ten years, and at the end of that period borrowed the stock again for another ten years. In borrowing the stock, respondent did not intend to make a profit from its sale but simply to encourage important employees of a company in which he held a 16% stock interest. When, in 1921, he had the opportunity of covering the short sale, and thereby realizing a profit of more than $1,500,000, he chose to forego his profit and instead to give to the employees Christiana stock worth $1,440,000.

These circumstances clearly justify the finding of the District Court that the payments "were beyond the norm of general and accepted business practice" and that "the course of conduct evoking them was in fact so extraordinary as to occur in the lives of ordinary businessmen not at all, and * * * in the business life of the plaintiff but once." See *Welch* v. *Helvering*, 290 U. S. 111.

II

Respondent is likewise not entitled to deduct the payments under Section 23 (b) as "interest paid

* * * on indebtedness." A loan of personal property is not normally regarded as giving rise to an "indebtedness" and payments to the lender equivalent to the return received by the borrower from the property are not normally regarded as "interest" on the loan. To the contrary, the popular import of the word "indebtedness" is an obligation to pay a sum of money, and the popular import of the word "interest" is an obligation to pay for the use of borrowed money. *Old Colony R. Co.* v. *Commissioner*, 284 U. S. 552, 560–561. The rule is established that it is the popular import of the words which controls construction of a tax statute. *Old Colony R. Co.* v. *Commissioner, supra*, and cases cited.

The payments made by respondent were neither periodical nor fixed in annual amount but were entirely dependent upon the profit or loss which the du Pont Company might enjoy or sustain. They reflected the corporate earnings of the du Pont Company rather than the use value of the property loaned to respondent by the Delaware Company.

Interest is generally charged by a lender in order to secure, for money lent, a return which he would not receive if the money remained idle in his possession. This factor is entirely absent in the present case. The Delaware Company would have been in precisely the same financial position if it had kept the du Pont stock as it was in after it made the loan to respondent. The purpose of the pay-

ments was not to secure to the Delaware Company a return on the property loaned which it would not have secured if it had kept the stock idle in its safe deposit box, but was rather to prevent the Delaware Company from being in any worse position as a result of the transaction.

There is no language in either respondent's contract with Christiana or in his contract with the Delaware Company which refers to the payments as "interest" or which shows any intention of the parties to the contract to regard the payments as interest. Section 23 (b) does not allow a deduction, as interest, of payments which the taxpayer himself did not regard as interest when he contracted to make them and which are not regarded as interest in the normal parlance of the business world.

ARGUMENT

INTRODUCTORY STATEMENT

The sole question involved in this case is whether the payments made by respondent to the Delaware Company fall within the provisions of paragraphs (a) or (b) of Section 23 of the Revenue Act of 1928. In the decision of this question two fundamental principles must be borne in mind: first, that a taxpayer claiming the benefit of a deduction must present a case coming squarely within the terms of the statute allowing the deduction (*New Colonial Co.* v. *Helvering*, 292 U. S. 435, 440; *White* v.

United States, 305 U. S. 281, 292; *Helvering* v. *Ind. Life Ins. Co.*, 292 U. S. 371, 381; *Woolford Realty Co.* v. *Rose*, 286 U. S. 319, 326); and second, that the language of the statute is to be read and construed in its natural and common meaning. *Welch* v. *Helvering*, 290 U. S. 111, 114; *Old Colony R. Co.* v. *Commssioner*, 284 U. S. 552, 560; *Woolford Realty Co.* v. *Rose*, *supra*, p. 327.

Applying these principles to the transaction here under review, we believe it to be demonstrably clear that respondent is not entitled to deduct the payments in question. We propose first to show that the payments do not come within the provisions of Section 23 (a), allowing a deduction for "ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." Our position is (1) that respondent's activities in connection with "conserving and enhancing his estate" did not constitute a business as that term is used in the statute, (2) that even if they did constitute a business, the expenses here involved were not paid or incurred in the conduct of that business, and (3) that in any event the payments were not "ordinary and necessary" in character. In the second portion of the brief we propose to show that the payments did not constitute "interest on indebtedness" within the meaning of Section 23 (b).

I

THE PAYMENTS ARE NOT DEDUCTIBLE AS ORDINARY AND NECESSARY EXPENSES PAID OR INCURRED IN CARRYING ON A TRADE OR BUSINESS

A. RESPONDENT'S ACTIVITIES IN CONNECTION WITH CONSERVING AND ENHANCING HIS ESTATE DID NOT CONSTITUTE A "TRADE OR BUSINESS"

The findings of the District Court set forth the activities of the taxpayer during the years 1919 to 1931 with reference to the business of the du Pont Company, of General Motors Corporation, and of other corporations in which respondent was a stockholder and director, and also with reference to the handling of his own investments (R. 220–221). These findings conclude with the statement that "The plaintiff's business was primarily that of conserving and enhancing his estate" (R. 221). This statement, although included as a part of the court's findings of fact, is, we believe, properly to be considered as a conclusion of law. The material *fact* is that a large part of the taxpayer's time and attention was devoted to the handling of his own investments. The question whether activities such as this can ever constitute the carrying on of a "business" within the meaning of Section 23 (a) is, in our view, not a question of fact but of statutory interpretation. The finding of the District Court on this matter, therefore, is entitled to no greater weight than its decision on the other issues of law involved.

The facts with reference to respondent's activities are not in dispute. He was not a trader or speculator. He had practically no investments in brokerage accounts and in 1931, the year for which the deduction is claimed, he made only 11 sales of securities (R. 26, 221). At all material times respondent was Chairman of the Board of the du Pont Company, a position in which he received $10,000 or $20,000 a year (R. 168). From 1920 to 1924 he was president of General Motors Corporation, receiving $100,000 for his services in that capacity (R. 167). He was a director of several large banks and industrial corporations (R. 220). In serving in these capacities he was clearly engaged in business—the business of the various corporations of which he was an officer or director. But the very extent of these business interests serves to negative the assumption that he was engaged in a "business" of "conserving and enhancing his estate" separate and distinct from the business of the corporations in which he had invested and which he served.

A sharp distinction exists between the activities of a trader or dealer in securities, who seeks to make a profit from continuous purchases and sales in the stock market, and the activities of an investor who, though changing his investments from time to time, does so not to make an immediate profit from the specific transactions of purchase and sale but to conserve and enhance the value of his estate by maintaining in his portfolio the type

of securities which he deems best from a long-run investment viewpoint. There is some basis for believing that there is such a "business" as trading or dealing in securities for the immediate profit to be derived from such trading. See *Dart* v. *Commissioner,* 74 F. (2d) 845 (C. C. A. 4th); *Bedell* v. *Commissioner,* 30 F. (2d) 622, 624 (C. C. A. 2d); *Sacks* v. *Commissioner,* 66 F. (2d) 308, 309 (C. C. A. 4th). But we do not believe that mere personal investment activities, no matter how engrossing, can ever properly be characterized as the conduct of a business.

Practically everyone who has any capital devotes some time and energy to the conservation and enhancement of that capital and to consideration of the prudence of his investments. In the normal case, this investment activity is clearly not the conduct of a business and any expense incurred in connection with such activity is not deductible as a business expense. *Kane* v. *Commissioner,* 100 F. (2d) 382 (C. C. A. 2d); see *Van Wart* v. *Commissioner,* 295 U. S. 112, 116, and cases cited; *Monell* v. *Helvering,* 70 F. (2d) 631 (C. C. A. 2d); *Bedell* v. *Commissioner,* 30 F. (2d) 622, 624 (C. C. A. 2d).[9]

[9] In accordance with this general principle, it is established that a commission paid as an incident to an investment transaction is not deductible as an ordinary and necessary business expense. *Hutton* v. *Commissioner,* 39 F. (2d) 459 (C. C. A. 5th); *Bonwit Teller & Co.* v. *Commissioner,* 53 F. (2d) 381, 384 (C. C. A. 2d); *Tonningsen* v. *Commissioner,* 61 F. (2d) 199 (C. C. A. 9th); *Briarcliff Investment Co.* v. *Commissioner,* 30 B. T. A. 1269.

Such investment expense is rather a personal expenditure, the deduction of which is specifically prohibited by the Revenue Act. Section 24 (a), *supra*, p. 3.

Certainly an active lawyer of moderate means who subscribes to a financial service in order to keep himself informed as to the prudence of his personal investments and as to the desirability of changing his portfolio from time to time, cannot deduct the cost of subscription to this service as an expense incurred in the "business" of conserving and enhancing his estate. His investment activities are personal and the cost of those activities is a personal expense. The activities of the taxpayer here are of precisely the same character as those of the lawyer in the case supposed; the difference is solely one of degree. Respondent, being a man of tremendous wealth, must naturally spend more time than the ordinary person in looking after his personal affairs. The fact that approximately 50% of respondent's time was so spent merely attests the extent of his investment interests. Similarly, the fact that he maintained a staff of employees in two offices to aid him in formulating his investment policy simply means that he believed his stake in prudent investment to be so large as to warrant intensive personal investigation and attention instead of reliance on financial and statistical services or on the advice of brokers.[8]

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[8] The fact that respondent acted as a director or officer of several corporations of which he was a stockholder is, we

However much time respondent spent on his affairs and however much expense he incurred in handling them, they remained personal activities serving no different economic function in the business world from that served by the personal investment of capital by the ordinary moderate investor. Certainly Congress did not intend to allow a wealthy taxpayer, whose investments necessarily generate more activity, to deduct investment expenses and to prohibit such deductions to the taxpayer of moderate means.

The rule established by the court below serves to obliterate the distinction between personal and business expenses. It permits respondent to convert purely personal and capital expenses into ordinary and necessary business expenses by the simple expedient of treating the conservation of his estate as a business and the cost of deferring liquidation of a personal indebtedness as an expense of the business. Adoption of this rule is not required by any binding authority.[10] We submit that it is

believe, immaterial to the question of whether he was engaged in a "business" of enhancing and conserving his estate. In acting as director, he was engaged in the business of the corporation, not in any business of his own. Insofar as such directorships furnished him with information enabling him to invest more prudently, they fall into the same category as the maintenance of a staff of employees for the same purpose.

[10] There is no decision of this Court directly upon the question. The ruling of the court below is, however, supported by several decisions of other Circuit Courts of Ap-

wrong in principle and so extremely inequitable in its favoritism to the wealthy as to repel the conclusion that it properly reflects the intent of Congress.

B. THE PAYMENTS WERE NOT EXPENSES PAID OR INCURRED IN CARRYING OUT RESPONDENT'S "BUSINESS" OF CONSERVING AND ENHANCING HIS ESTATE

If we are correct in believing that investment activities in connection with conserving and enhancing one's own capital do not constitute a "business," respondent is admittedly entitled to no deduction under Section 23 (a). Even if we are in error as to this, however, respondent is entitled to no deduction under that section unless the expenses were proximately connected with this "business" and unless they were "ordinary and necessary" in character. In our view the payments do not meet either test.

The court below, adopting the District Court's finding that respondent was engaged in the business of conserving and enhancing his estate, held that payments made by him to the Delaware Company were made in connection with that business. The court reasoned that in 1931 respondent had an

peals and of the Board of Tax Appeals. *Kales* v. *Commissioner*, 101 F. (2d) 35 (C. C. A. 6th); *Miller* v. *Commissioner*, 102 F. (2d) 476 (C. C. A. 9th); *Foss* v. *Commissioner*, 75 F. (2d) 326 (C. C. A. 1st); *von Echt* v. *Commissioner*, 21 B. T. A. 702, 27 B. T. A. 1419; *Kissel* v. *Commissioner*, 15 B. T. A. 1270. These decisions we believe to be unsound. Looking the other way are the cases cited at p. 24, *supra*.

obligation to the Delaware Company which, regardless of its origin, he had to meet either by return of the borrowed du Pont stock or by making the payments here in question. Return of the stock would have involved serious depletion of his estate; making the payments, on the other hand, conserved the estate by deferring liquidation of the indebtedness. Since the payments served to conserve the estate and since conservation of the estate was respondent's business, the conclusion inevitably followed that the payments were deductible as ordinary and necessary business expenses.

This approach, we submit, is deceptively simple. We believe it elementary that, even if there is such a businss as conserving one's estate, every payment on a personal obligation which defers its liquidation and thereby prevents depletion of the estate is not an expense paid or incurred in connection with that business. For example, if respondent had borrowed the du Pont stock from the Delaware Company in order to give it to his friends, or in order to pay gambling debts, or for the satisfaction of some other personal desire, it is plain that the payments here in question would not be deductible as a business expense even though they tended to conserve respondent's capital. Deductibility, therefore, does not depend upon the immediate effect of the payments upon respondent's financial position but rather upon the purpose and history of the obligation pursuant to which the payments were made.

Cf. *Menihan* v. *Commissioner*, 79 F. (2d) 304 (C. C. A. 2d), certiorari denied, 296 U. S. 651; *Cripple Creek Coal Co.* v. *Commissioner*, 63 F. (2d) 829 (C. C. A. 7th).[11] In ignoring these factors the court below committed critical error.[12]

The correct approach was, we believe, taken by the Board of Tax Appeals in *du Pont* v. *Commissioner*, 37 B. T. A. 1198, 1266, a case involving the deductibility of payments made by the respondent to the Delaware Company in 1929 pursuant to precisely the same contract which is here under re-

[11] In *Menihan* v. *Commissioner*, the court rejected the taxpayer's claim that he had suffered a loss because he had made payment, without recourse, upon a liability which at the time of payment was his own liability. The court inquired into the history of the liability and determined that originally the taxpayer had endorsed a corporation note to protect his investment in its stock and that the creditors' adjustment which made the liability his own primary debt without recourse was part of an arrangement which preserved the value of his shares and represented a capital contribution. Similarly in the *Cripple Creek Coal Co.* case the court held that certain payments were not ordinary and necessary expenses since in substance they represented installments in satisfaction of a debt owing to a customer because of its advances toward the cost of a spur track and were therefore a capital investment.

[12] It is well established that component steps of a single transaction are to be viewed as a whole and may not be treated separately for tax purposes. *Commissioner* v. *Ashland Oil & R. Co.*, 99 F. (2d) 588, 591 (C. C. A. 6th), certiorari denied, 306 U. S. 661; *Starr* v. *Commissioner*, 82 F. (2d) 964, 968 (C. C. A. 4th), certiorari denied, 298 U. S. 680; *Ahles Realty Corp.* v. *Commissioner*, 71 F. (2d) 150, 151 (C. C. A. 2d); *Prairie Oil & Gas Co.* v. *Motter*, 66 F. (2d) 309, 311 (C. C. A. 10th).

view. In holding that the payments were nondeductible the Board stated (p. 1274):

> The expense must be paid or incurred in trade or business—petitioner's business—which means that it must be not merely connected in some way with, but must be directly and proximately connected with petitioner's assumed business of an investor, managing investments. *Kornhauser* v. *United States*, 276 U. S. 145. Merely because he was such investor does not per se make any sort of borrowing of corporate stock in which he invests a part of his business, or make expense in so doing an expense incurred in his business; it might be in a transaction wholly unrelated to his business. It might be, for instance, a part of a transaction of donation to some eleemosynary institution and the basis for deductible contributions—patently without the requisite of proximate and direct business connection. * * * We therefore cannot disregard the setting, the reasons for entering into the transaction for borrowing stock; to do so would leave before us a mere borrowing, isolated from the business which we have assumed petitioner to be carrying on. * * *

Certainly borrowing in one form or another is proximately connected with the conduct of a great many businesses. But in order to determine whether there is such a proximate connection in any particular case it is clearly necessary to inquire into all the facts occasioning the borrowing.

Determination of whether respondent's payments to the Delaware Company were made in carrying on respondent's business as an investor depends, therefore, upon the origin of the liability pursuant to which the payments were made. On principles settled by this Court respondent is entitled to a deduction only if the creation of this liability was a proximate result of or was directly connected with his business. *Kornhauser* v. *United States*, 276 U. S. 145, 153. It is not enough that the liability was incurred in connection with the business of a corporation in which respondent held stock; respondent may receive the deduction only if the liability was incurred in connection with the conduct of his own business. *Dalton* v. *Bowers*, 287 U. S. 404; *Burnet* v. *Clark*, 287 U. S. 410; *Burnet* v. *Commonwealth Imp. Co.*, 287 U. S. 415; *Van Dyke* v. *Helvering*, 291 U. S. 642.

In *Burnet* v. *Clark, supra*, this Court held that losses suffered by a majority stockholder and officer, through endorsement of obligations of the corporation, were not losses attributable to the taxpayer's business even though intended to preserve the value of his investment in the capital shares of the corporation. The Court stated (p. 415):

> The respondent was employed as an officer of the corporation; the business which he conducted for it was not his own. There were other stockholders. And in no sense can the corporation be regarded as his *alter*

> *ego*, or agent. He treated it as a separate entity for taxation; made his own personal return and claimed losses through dealings with it. He was not regularly engaged in endorsing notes, or buying and selling corporate securities. The unfortunate endorsements were no part of his ordinary business, but occasional transactions intended to preserve the value of his investment in capital shares.

This decision exemplifies the general principle that expenditures made in the best interests of a corporation and intended to benefit the taxpayer only through his stockholdings in the corporation are capital in nature. They may not be deducted as losses (*Mastin* v. *Commissioner*, 28 F. (2d) 748 (C. C. A. 8th); *Menihan* v. *Commissioner*, 79 F. (2d) 304 (C. C. A. 2d), certiorari denied, 296 U. S. 651; *Park* v. *Commissioner*, 58 F. (2d) 965 (C. C. A. 2d), certiorari denied, 287 U. S. 645), and, under the doctrine of *Burnet* v. *Clark*, they may not be deducted as business expenses. *Bing* v. *Helvering*, 76 F. (2d) 941, 942 (C. C. A. 2d).

In *Mastin* v. *Commissioner, supra*, for example, the taxpayer paid for advertising real estate owned by a corporation in which he was a stockholder. The court held that the payment was not a deductible item even though serving to enhance the value of the taxpayer's stock, stating (p. 753):

> The payment was therefore made, not by petitioner to advertise his own real estate,

> not by the corporation to advertise real estate owned by it, but by petitioner as a voluntary one. It was, in our opinion, a capital expenditure, which might enhance the value of petitioner's stock by increasing the value of the lands of the corporation.

These decisions plainly govern the present case. Respondent's purpose in his entire course of conduct was to secure for the du Pont Company an efficient management (R. 212–213, 215–217, 221, 229). This was obviously the business of the du Pont Company itself. Indeed, respondent's personal participation, at the instance of the company, came only after the initial proposal that the company itself sell shares to the members of the executive committee was found legally objectionable (R. 210–211). It is true that an efficient management for the company would enhance the value of respondent's investment in the company, but this was, of necessity, a secondary consideration. It should be remembered that respondent was the beneficial owner of but 16% of the stock of the company. Had his primary purpose been to enhance the value of his estate, he would obviously not have entered into a transaction from which 84% of the benefit went to others. Moreover, when, in 1921, the price of du Pont stock had decreased to approximately one-half of the price at which respondent had sold it to the committeemen in 1919, he immediately gave to the committeemen shares of Christiana stock of a total value of $1,440,000

in order to compensate them for any loss from their stock purchases. It can scarcely be claimed that such a gift was made in carrying out respondent's investment business. To the contrary, that gift, like the expenditures here involved, was part of a single plan which, as the District Court found,[13] was entered into to benefit the business of the corporation and which was not proximately connected with respondent's business of enhancing his investments. *Kornhauser* v. *United States, supra;* cf. *Kenan* v. *Bowers,* 50 F. (2d) 112 (C. C. A. 2d).

C. THE PAYMENTS WERE NOT "ORDINARY AND NECESSARY" EXPENSES

Even if respondent's investment activities did constitute a business and even if the payments here in question were paid or incurred in carrying out that business, he is entitled to no deduction under Section 23 (a) unless the payments were "ordinary and necessary" expenses. We believe that they were neither.

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[13] In its opinion the District Court stated (R. 235): "* * * one might bring the payment of funds by the plaintiff one stage closer to the ultimate result sought by him, without rendering such sums deductible. For example, if the plaintiff, out of his own pocket, had increased the pay of chemists employed by the du Pont Company with the hope that by reason of such increase they would work more effectively to improve the processes of the du Pont Company, perhaps thereby increasing the value of the plaintiff's stock, I conceive that it would not be contended that these payments would be deductible by the plaintiff from his gross income under the theory here advanced by him."

It was neither ordinary nor necessary for the conduct of respondent's "business" of conserving and enhancing his estate for him to have incurred a large liability in order to compensate employees of a company in which he held stock. There is no finding of the District Court, and no evidence in the record, that respondent was required to incur this liability in order to conserve and enhance the value of his du Pont stock. The burden of providing adequate compensation for the members of the executive committee rested upon the company and respondent does not suggest that the company was financially unable to discharge that obligation. The fact that respondent undertook to assume the burden himself cannot change what would have been an ordinary and necessary business expense of the corporation into an ordinary and necessary business expense of one of its stockholders. And any contention that it was necessary for respondent to continue the liability, once incurred, is conclusively refuted by the fact that, in 1921, he could have liquidated his obligation at a tremendous profit (see pp. 8–9, *supra*).

Moreover, the liability with respect to which the payments were made had its origin in what was essentially a short sale of securities—a sale of borrowed stock. While short sales are frequently made by dealers or traders in securities, they are not ordinarily made by one whose "business" is simply the conservation and enhancement of his estate. It is conceded in this case that respondent

was not a dealer or trader in securities and did not devote his time to buying and selling stock through brokers as a matter of speculation. The record shows that he did not ordinarily enter into short sales and in fact knew little about them. Under these circumstances, payments made in connection with a short sale cannot be regarded as an ordinary and necessary expense of carrying on respondent's business. *Terbell* v. *Commissioner,* 71 F. (2d) 1017 (C. C. A. 2d), affirming, *per curiam,* 29 B. T. A. 44.

Even as a short sale, the transaction was obviously out of the ordinary. The usual short sale is a short-term proposition entered into by a trader or speculator in securities in order to make a profit out of the specific transaction. *Cf. Provost* v. *United States,* 269 U. S. 443. Here, although respondent used the mechanics of a short sale, he borrowed the stock which he sold for a period of ten years and at the end of that period borrowed the stock again for another ten years. In borrowing this stock respondent did not have the intent of making a profit from its sale but simply desired to encourage important employees of a company in which he held a 16% stock interest. When, in 1921, he had the opportunity of covering the short sale and thereby realizing a profit of more than a million and a half dollars, he chose instead to give to the committee Christiana stock worth $1,440,000. Certainly it is most unusual, and clearly unnecessary, for a stockholder having

but a 16% interest in a corporation, to give to its employees $1,440,000 and to forego realizing a profit of somewhat more than that, in order to conserve and enhance his investment in the company.

These circumstances seem to us clearly to justify the finding of the District Court (R. 235) that the payments here involved "were beyond the norm of general and accepted business practice," and that "the course of conduct evoking them was in fact so extraordinary as to occur in the lives of ordinary business men not at all, and * * * in the business life of the plaintiff but once."

The decision of the Board of Tax Appeals in the case involving respondent's 1929 payments to the Delaware Company is in accord with the conclusion of the District Court (*du Pont* v. *Commissioner*, 37 B. T. A. 1198). The Board stated (pp. 1274–1275):

> This was no ordinary investment, but an extraordinary situation, which cannot be allocated within the confines of the ordinary business of, or cause an ordinary expense of, an investor managing his investments. Plainly, an investor does not ordinarily find it necessary to encourage the employees or executives of a corporation in which he invests by borrowing and selling to them large amounts of stock for their encouragement. Indeed, the very fact that it was the petitioner, a stockholder, instead of the du Pont Co. itself (which had intended to encourage the executives, but could not constitutionally do so), thus encouraging the executives of

> that company, seems sufficient indication that the situation was extraordinary. * * * We find it unnecessary, in view of this conclusion, to decide whether the expense was necessary.

A somewhat analagous situation was presented to this Court in *Welch* v. *Helvering*, 290 U. S. 111. There the taxpayer, a former officer of a bankrupt corporation, had made payments on the debts of the corporation after its discharge from bankruptcy in order to strenghen his own business standing and credit. This Court held that although these were business expenses, and perhaps necessary, they were not "ordinary" in character and were therefore not deductible. Mr. Justice Cardoza, speaking for the Court, stated (p. 114):

> Men do at times pay the debts of others without legal obligation or the lighter obligation imposed by the usages of trade or by neighborly amenities, but they do not do so ordinarily, not even though the result might be to heighten their reputation for generosity and opulence. Indeed, if language is to be read in its natural and common meaning (citing cases), we should have to say that payment in such circumstances, instead of being ordinary is in a high degree extraordinary. There is nothing ordinary in the stimulus evoking it, and none in the response. * * *

That case controls the decision here. If it is unusual for a man to pay barred debts of a cor-

poration in order to reestablish his credit, it is certainly equally extraordinary for a comparatively small stockholder in a corporation to expend millions of dollars, not to make a profit from the expenditure, but in order to give the executive committee of the corporation an interest in the business.

Dart v. *Commissioner,* 74 F. (2d) 845 (C. C. A. 4th), upon which respondent relies, is entirely distinguishable. The taxpayers there were engaged in the business of trading in stock on the New York Stock Exchange and in the usual course of that business they made short sales.[14] The holding of the court was merely that expenditures made for the purpose of continuing to hold stock borrowed for short-sale transactions were deductible as ordinary and necessary expenses paid "in order to carry on the business of making 'short sales'." The vital differences between that case and the present one are obvious: the respondent was not engaged in business as a trader or dealer in securities but merely in the "business" of conserving and enhancing his estate; he did not make short sales in the usual course of his business, and in fact knew little about them; and he made the short sale here

[14] The court pointed out (p. 846) that the taxpayers had made hundreds of purchases and sales during the taxable year, that the total selling price of stocks sold during the year by one taxpayer was $56,945,192.51, and by the other was $3,456,302.50, and that many of the accounts maintained by the taxpayers were so-called "short" accounts.

involved not to maintain his position in the market but primarily to benefit a corporation in which he held stock. Under all of the authorities above cited, a short sale made under such circumstances is not an ordinary and necessary business transaction.

II

THE PAYMENTS ARE NOT DEDUCTIBLE AS INTEREST PAID ON INDEBTEDNESS

Respondent urges that, even if the payments in question were not ordinary and necessary business expenses deductible under Section 23 (a), they constituted "interest paid * * * on indebtedness" deductible under Section 23 (b). The District Court in the present case (R. 240–241) and the Board of Tax Appeals in respondent's 1929 case (37 B. T. A. at 1272–1273) rejected the contention; it was not considered by the court below. We believe the contention to be wrong in principle and without support in authority.

One does not normally think of a loan of personal property as giving rise to an "indebtedness," nor of payments to the lender equivalent to the return received by the borrower from the property as "interest" on the loan. To the contrary, the popular import of the word "indebtedness" is an obligation to pay a sum of money and the popular import of the word "interest" is the amount one has contracted to pay for the use of borrowed

money."[15] *Old Colony R. Co.* v. *Commissioner*, 284 U. S. 552, 560, 561; *Maryland Casualty Co.* v. *Omaha Electric L. & P. Co.*, 157 Fed. 514, 519 (C. C. A. 8th); *Title Guaranty & Surety Co.* v. *Klein*, 178 Fed. 689, 690 (C. C. A. 3rd); *Westerfield* v. *Rafferty*, 4 F. (2d) 590, 594 (E. D. N. Y.); *Kishi* v. *Humble Oil and Refining Co.*, 10 F. (2d) 356 (C. C. A. 5th); *Corbett Investment Co.* v. *Helvering*, 75 F. (2d) 525, 528 (App. D. C.); *City of Lincoln, Neb.* v. *Ricketts*, 77 F. (2d) 425, 428 (C. C. A. 8th); *Baltimore & O. R. Co.* v. *Commissioner*, 78 F. (2d) 460, 462–463 (C. C. A. 4th); *The Dry Dock Bank* v. *The American Life Ins. and Trust Co.*, 3 N. Y. 344, 355; *Hayes* v. *Commissioner*, 261 Mass. 134; *Fall River Electric Light Co.* v. *Commissioner*, 23 B. T. A. 168; *New Orleans Land Co.* v. *Commissioner*, 29 B. T. A. 35; *Terbell* v. *Commissioner*, 29 B. T. A. 44 affirmed *per curiam*, 71 F. (2d) 1017 (C. C. A. 2d). And the rule is established that it is the popular import of the words which controls construction of a tax statute. *Old Colony R. Co.* v. *Commissioner*, 284 U. S. 552, 560; *Maillard* v. *Lawrence*, 16 How. 251, 261; *De Ganay* v. *Lederer*, 250 U. S. 376, 381.

The decision of this Court in *Old Colony R. Co.* v. *Commissioner*, *supra*, supplies the guiding prin-

[15] It is worthy of note that the Delaware law regarding "rates of interest" applies only to payments "for the loan or use of money." Delaware Revised Code, 1935, Sec. ~~[illegible]~~. 3101

ciple. In that case the Court, after stating the fundamental proposition that "The popular or received import of words furnishes the general rule for the interpretation of public laws" (p. 560), continued as follows (pp. 560–561):

> * * * as respects "interest," the usual import of the term is the amount which one has contracted to pay for the use of borrowed money. * * * We cannot believe that Congress used the word having in mind any concept other than the usual, ordinary and everyday meaning of the term * * *.

This rule has consistently been followed by the lower federal courts, by the state courts and by the Board of Tax Appeals (see cases cited, p. 41, *supra*). For example, in *New Orleans Land Co.* v. *Commissioner, supra,* it is stated (pp. 38–39):

> We think it follows that if there was no debt, no money withheld, and no obligation to pay money, there was no agreement, contract or obligation to pay interest.

Similarly, in *Fall River Electric Light Co.* v. *Commissioner, supra,* the Board of Tax Appeals defined interest as follows (p. 171):

> Interest on indebtedness has a definite and well accepted meaning as "the compensation allowed by law or fixed by the parties for use, or forbearance, or detention of money."

In his brief in the court below, respondent did not deny that the popular meaning of the words "interest on indebtedness" is compensation paid for the use or forbearance of money; his argument

consisted largely of a discussion of the classical meaning of interest as developed in the old Roman law (Br., pp. 20–23). This discussion concluded with the statement (p. 23) that "the real question is whether we should impute to Congress the intention to substitute the narrower popular meaning for the broader classical usage when inherent reasonableness requires the use of the latter."

The answer to this "real question" is, as we have pointed out, furnished by the decision in *Old Colony R. Co.* v. *Commissioner,* 284 U. S. 552, where this Court, citing many authorities, held that the language of a tax statute is to be construed in accordance with its popular meaning and not in accordance with any technical—or classical—meaning which might be ascribed to it. The Court aptly quoted from the decision in *Lynch* v. *Alworth-Stephens Co.,* 267 U. S. 364, 370, as follows:

> * * * the plain, obvious and rational meaning of a statute is always to be preferred to any curious, narrow, hidden sense that nothing but the exigency of a hard case and the ingenuity and study of an acute and powerful intellect would discover.

Respondent's statement that "inherent reasonableness" requires construction of the statute to allow the deduction here claimed is based on the theory that the payments to the Delaware Company on the loan of the stock were economically similar to interest paid on an indebtedness and should, therefore, be treated in the same manner

for tax purposes. This economic similarity may be assumed for purposes of the argument but its assumed existence does not alter the character of the payments or bring them within the four corners of the statute. Cf. *New Colonial Co.* v. *Helvering*, 292 U. S. 435, 440; *White* v. *United States*, 305 U. S. 281, 292. *Helvering* v. *Ind. Life Ins. Co.*, 292 U. S. 371, 381; *Woolford Realty Co.* v. *Rose*, 286 U. S. 319, 326. It is unnecessary to debate the question whether Congress should have provided for the deduction of payments made on a loan of personal property; the fact is that it did not do so. The wisdom of limiting the deduction to "interest paid on indebtedness" is, as the Board of Tax Appeals stated in respondent's 1929 case, "a problem for the legislative body and not for us" (37 B. T. A. at 1279.

The principal authority cited by respondent in his brief in the court below was *Brush-Moore Newspapers, Inc.* v. *Commissioner*, 37 B. T. A. 787. The case is entirely distinguishable. The taxpayer corporation there, being in financial difficulties and desiring to avoid annual principal payments of $50,000 on notes which it had given, issued 4,000 shares of its own second preferred stock in exchange for $400,000 of the notes. The exchange agreement provided that if dividends on this second preferred stock were not paid in any quarter, a fixed amount should be paid as interest, and, in addition, such amount as the directors of the corporation deemed necessary for the support and

maintenance of the payee of the notes or his wife, the payee being guaranteed by the taxpayer against any loss resulting from the exchange. In concluding that "dividends" on this preferred stock were in reality interest payments, the Board referred to prior decisions, and particularly to *Richmond, Fredericksburg & Potomac Railroad Co. v. Commissioner*, 33 B. T. A. 895, affirmed, 90 F. (2d) 971 (C. C. A. 4th), where, in determining that fixed periodical payments made to holders of "guaranteed stock" were in reality interest payments, it stated (pp. 898-899):

> It seems to us, however, that in this case the basic test to be applied is whether the stockholder invested his money with the view of receiving a return from its use dependent on the successful operation of the company, on the one hand, or, on the other hand, whether he invested with no regard to the profit or loss which the company might enjoy or sustain, but with a dependence on the regular payment of compensation for the use of the money and an assurance of its ultimate repayment. * * *

In the present case, the payments made by respondent were entirely dependent upon the profit or loss which the du Pont Company might enjoy or sustain. They were neither periodical nor fixed in annual amount and reflected the corporate earnings of the du Pont Company rather than the use value of the property loaned to respondent by the Delaware Company.

Interest is generally charged by a lender in order to secure, on money loaned, a return which he would not receive if the money remained idle in his possession. It is significant that this factor is entirely absent in the present case. The Delaware Company would have been in precisely the same financial position if it had kept the du Pont stock as it was in after it made the loan to respondent. The purpose of the payments was not to secure to the Delaware Company a return on the property loaned which it would not have secured if it had kept the stock idle in its safe-deposit box, but was rather to prevent the Delaware Company from being in any worse position as a result of the transaction. This clearly indicates that the payments here in question, unlike normal interest payments, did not in any real sense constitute compensation for the "use or forbearance" of the subject matter of the loan.

It should be noted that there is no language in either respondent's contract with Christiana or in his contract with the Delaware Company which refers to the payments as "interest" or which shows any intention on the part of the parties to the contract to regard the payments as interest. We submit that it would be inconsistent with the whole philosophy of the tax law to allow a deduction as interest of payments which the taxpayer himself did not regard as interest when he contracted to make them, and which, as we have shown

above, are not regarded as interest in the normal parlance of the business world.

CONCLUSION

The decision of the court below should be reversed.

Respectfully submitted.

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